Westlaw Delivery Summary Report for 1,USER

Date/Time of Request:	Thursday, October 17, 2013 08:02 Central
Client Identifier:	WLILAWSCHOOL
Database:	UK-TRANS
Citation Text:	2008 WL 2872582
Lines:	1024
Documents:	1
Images:	0

Official Receiver v Stephen Richard Key

No. 6NG15675

Nottingham County Court

His Honour Judge Mithani

Wednesday, 19th March 2008

Representation

- Mr. P. Capon (instructed by Wragge & Co.) appeared on behalf of the Claimant.
- Mr. S. Whitaker (instructed by Brindley Twist Tafft & James) appeared on behalf of the Defendant.

Judgment

His Honour Judge Mithani:

1 This is an application by the Official Receiver for a disqualification order against the Defendant, Stephen Richard Key, pursuant to section 6 of the Company Directors Disqualification Act 1986 , arising as a result of his conduct as a director of Riva Interiors Limited. I will refer to Riva Interiors Limited in the course of this judgment as 'Riva'.

2 Section 6(1) of the Company Directors Disqualification Act 1986 provides:

"The court shall make a disqualification order against a person in any case where on an application under this section it is satisfied:(a)that he is or has been a director of a company which has at any time become insolvent (whether while he was a director or subsequently); and(b)that his conduct as a director of that company (either taken alone or taken together with his conduct as a director of any other company or companies) makes him unfit to be concerned in the management of a company."

3 Riva was incorporated on 28th August 2003 and was compulsory wound up on 1st December 2004 on the petition of a trade creditor, CIF Limited, presented on 18th October 2004. Riva was engaged in business as a contractor in the construction industry. Its work primarily included interior glazing and partitioning. However, it undertook other work as well, such as installing mezzanine floors and other internal partitions and divisions. I need not deal in detail with the manner in which Riva transacted its business. That is set out in detail in the evidence filed in these proceedings and is not in issue.

4 Trading commenced around the time of incorporation. The Defendant was appointed a director on incorporation. On 2nd September 2003, a Peter Ian Balch was appointed an additional director. On 12th December 2004, a William Leslie Smith was also appointed a director. Mr. Smith resigned as a director in January 2004. Mr. Balch alleges that he resigned his directorship on 5th July 2004. However, the Defendant does not accept that Mr. Balch resigned his directorship. He maintains that Mr. Balch continued to be a director until Riva was wound up on 1st December 2004.

5 Riva traded from premises at 35 Park Row, Nottingham, which was also its registered office. The Defendant funded the start up of Riva with £5,000 and held 80% of the issued share capital of Riva. Mr. Balch invested no money in the company. However, he held the remaining 20% of the issued share capital of Riva.

6 Riva succeeded in winning a few small contracts in 2003. In 2004, Riva won a larger contract, worth in the region of £150,000, from a main contractor, Bower &Kirkland, in relation to work that it was commissioned to do at the Experian Headquarters in Nottingham. It also won another contract from Winfield Construction worth some £40,000.

7 Difficulties arose in the completion of the Bower &Kirkland contract that caused Riva's costs to rise, which it could not recover. Riva ran

out of money and ceased to trade in September 2004. A winding up petition was presented on 18th October 2004 and the winding up order was made on 1st December 2004.

8 Riva did not trade long enough for any year-end accounts to be prepared. Its accounting records indicate that for the 12 months to the end of August 2004, it had a turnover of some £130,000 and made a trading loss of some £110,000. In the period from 1st September 2004 to the cessation of trading, Riva's accounting records indicate additional turnover of some £67,000 and a further trading loss of some £30,000.

9 The Official Receiver did not seek the preparation and completion of a statement of affairs, following the liquidation of Riva, either from the Defendant or from Mr. Balch. However, his examination of the records of Riva and the enquiries conducted into its financial affairs indicate that at the date of its liquidation, Riva had no assets. Its liabilities to creditors came to over £123,000, of which PAYE/NIC amounted to some £31,000 and trade creditors some £83,000.

10 There is no issue that the Defendant was, at all relevant times, a director of Riva, and that accordingly the requirements at s.6(1)(a) are satisfied.

11 The Official Receiver makes two separate allegations against the Defendant by reason of which he contends that the conduct of the Defendant as a director of Riva makes him unfit to be concerned in the management of a company.

12 The first is that the Defendant caused Riva to trade to the detriment of the Crown — that is the Inland Revenue — in respect of non payment of PAYE and NIC. During its period of trading, from August 2003 to September 2004, Riva deducted PAYE and NIC from its employees totalling some £33,000 but only paid over to the Inland Revenue the sum of £1,384.

13 The second is that the Defendant caused Riva to trade to the detriment of a major supplier, Curston (Radstock) Limited — which I will refer to as ‘Curstons’ in the course of my judgment — in that despite Riva being indebted to Curstons in the sum of £21,000 by September 2004, no attempt was made to make any payment of — or towards — this sum. Instead, monies received by Riva in August and September 2004 were paid out to other creditors, including a company that was wholly owned — or controlled — by the Defendant called Riva Art Stone Limited. I will refer to Riva Art Stone Limited in the course of this judgment as ‘Art Stone’.

14 The allegations that the Official Receiver makes are summarised at para.66 of the first report of the Deputy Official Receiver, Erica Vivian Church, dated 30th November 2006 in support of the application. I will refer to Miss Church in the course of this judgment as ‘the Deputy Official Receiver’.

15 Para.66 states that:

“With regard to the affairs of Riva Interiors Limited, the following are matters by reference to which Stephen Richard Key is in the opinion of the Secretary of State unfit to be concerned in the management of a limited company …” The Deputy Official Receiver summarises the first allegation in the following terms:

“Mr. Key caused Riva to trade to the detriment of the Crown from commencement of trading in August 2003 to cessation of trading in September 2004. In particular …” She then sets out a number of bullet points in support of that assertion:

• • “Riva traded as an interior furnishing and partitioning contractor between August 2003 and September 2004.”
• • “Based on records maintained by Riva, the total amounts due in respect of PAYE/NIC during the whole period of trading was £39,608. This amount was deducted from employees' wages by Riva.”
• • “This amount was reduced to £33,018 following set off and CIS deductions applied.”
• • “As at cessation, the company had paid £1,384 to the Inland Revenue in respect of this liability, leaving £31,634 outstanding at liquidation.”

• • "During the period August 2003 to closure of Riva's bank account in November 2004, £278,610 was paid out of Riva's bank account, of which only £1,384 was paid to the Inland Revenue and the balance to various third parties, including employees and associated companies".

16 The Deputy Official Receiver summarises the second allegation in the following terms:

"Mr. Key caused Riva to trade to the detriment of a major supplier in August and September 2004. In particular …"

• • "Throughout August and September 2004, Curstons, who were owed £20,960, were pressing Riva for payment."
• • "Mr. Key made representations to Curstons that payment would be made once an expected payment from a customer was received by Riva. As a result of this and other representations made by both Mr. Key and another Riva employee, Curstons put on hold legal action to recover the debt."
• • "When the payment to which Mr. Key referred was received by Riva, it was not paid to Curstons. Instead £10,000 was transferred to Mr. Key's personal bank account, £2,232 was used to make a payment on account of another supplier, £4,703 was used to pay wages and salaries, and £10,296 was recorded as being transferred into the inter company account via petty cash."
• • "On 31st October 2004, notwithstanding the failure of Riva to make payments to Curstons, it ordered goods to the value of £16,602 from Lee Glass. No payments appear to have been made in respect of this debt. As at the date of winding up £26,602, was owed to Lee Glass and £20,960 was owed to Curstons. Between them, the two suppliers represent 52% of the total liabilities to trade creditors."
• • "During August and September 2004, at the time when Curstons were pressing for payment, £32,300 was transferred to an associated company of which Mr Key was sole director. Of this, £10,600 was transferred after the order had been placed with Lee Glass."

17 It is necessary that I clarify a few of the matters that are referred to in the summary that I have just read out. First, it is accepted by the Official Receiver, for the purpose of these proceedings, that Riva is entitled to credit in the sum of some £5,000 against the amount that is alleged to be due to the Inland Revenue. The reason for that entitlement is set out in para.23 of the Defendant's witness statement dated 11th June 2007. As the Official Receiver accepts that Riva is entitled to credit for that sum, the matter does not require any further mention by me.

18 Second, although the sum of £10,000 was transferred to the Defendant's account, as alleged by the Deputy Official Receiver, it was repaid by the Defendant to Riva a few days after it was transferred to him. The amount of £10,000 was transferred to the Defendant's account on 10th September 2004 and was repaid by the Defendant to Riva on 27th September 2004.

19 Third, although the penultimate bullet point set out in para.66 of the Deputy Official Receiver's report refers to an outstanding debt due from Riva to Lee Glass of some £26,600, it is no part of the Official Receiver's case that the Defendant caused or allowed Riva to trade to the detriment of Lee Glass. This is because Lee Glass do not support either allegation of misconduct made by the Official Receiver against the Defendant. Indeed, the exhibit to the Defendant's written evidence includes a letter from Lee Glass in which, among other things, Lee Glass confirm that the Defendant has at all times behaved, to use their words 'in an entirely honest and ethical manner' towards them. They have no complaints at all about the manner in which the Defendant conducted the affairs of Riva, despite what is plainly a substantial sum that is due to them from Riva, which it is clear they have no prospect of being able to recover in the liquidation of Riva.

20 The Official Receiver's case against the Defendant initially appeared to be based on Mr. Balch's statement to the Official Receiver's examiner made on 11th June 2005, in which Mr Balch sought to place responsibility for the main control of the financial affairs of Riva with the Defendant. In that statement Mr. Balch said this:

"As far as the company was concerned, I looked after sales, clients, and dealing with purchasers, and Mr. Key was responsible for the financial side of the company. I was a signatory to the bank account but did not have control of the cheque book over the last three to four months. I received a salary of £40,000. I had no other benefits, but I didn't always receive my monthly wage. I was assured that I would be repaid outstanding overtime and expenses but have not been. My belief was that both VAT and PAYE were paid by Mr. Key, who dealt with Customs and Inland Revenue. I think the main difficulty was the lack of working capital as well as cash flow".

21 Mr. Balch provided a further statement to the Official Receiver's examiner on 23rd March 2006. It purports to give a fuller explanation of the matters referred to in his earlier statement. It is right that I read that statement out:

"With regard to my role as a director of Riva Interiors Limited, my job was to deal with every day operations of the trading side of the business. This meant that I was both on site and in the office. I would negotiate with customers and clients and deal with telephone queries regarding information and collection of monies due. I would put in application for payments to contractors we were working for. I would refer creditors to Mr. Key who were needing to be paid. I would always refer to Mr. Key as regards the payment of creditors.

As far as the PAYE and NIC were concerned, it was my belief that these funds were being paid. I was aware that they were late, and although I was aware I believed that Mr. Key was organising the payments as and when required.

My position in the company was as operations director/manager. In July 2004, I resigned as a director due to lack of support from Mr. Key, who had given the impression that he was going to invest funds in the company from personal funds, but none of this materialised. I continued to work as an employee and continued to assist with the operation of the company and the collection of monies due. However, as far as any queries as regards the finances, I would pass these on to Mr. Key for him to deal with. It became evident that he, Mr. Key, did not make these contacts and the queries then came back to me. Again, I would refer all matters to Mr. Key.

As far as Art Stone was concerned, I was aware of its existence. This company was, I understand, originally owned by Mr. Key's father-in-law. Mr. Key purchased it, I believe, from his father-in-law, I think, in early 2004. Mr. Key was a sole director as far as I knew. I had nothing to do with the company. I was not aware that transfers were being made from Riva to Art Stone. As far as I know, the company Art Stone Limited produced cast stone products for the construction industry, mainly housing. I have no other information concerning the company other than to say that it had its operating premises up in Yorkshire, near to Bradford. As far as I know it did not business with Riva Interiors".

22 The Defendant has filed and served written evidence in opposition to the Official Receiver's written evidence in support of the application. He has sought to do so in the form of a witness statement verified by a statement of truth, though — and the Official Receiver quite properly takes no point on this — he should have done so in the form of an affidavit.

23 The Defendant does not accept what Mr. Balch says. He says the precise opposite. At para.6 of his witness statement dated 11th June 2007 he says this:

"I strongly disagree with the statements that Mr. Balch had no involvement with any banks and that Mr. Key was responsible for the financial side of the company and that Mr. Balch did not have control of the cheque book. The facts are that:(a)Mr. Balch, together with his assistant, Elaine Lovett, ran all aspects of the administration of the Company's affairs from its office at Cumberland House, Park Row, Nottingham. There they had the Company's accounting records, which were kept on the Sage Line 50 software package, and Mr. Balch, or Elaine under his supervision, were responsible for making all entries in those accounts. These, of course, in-

clude entries relating to the bank account, which has to be reconciled to the other accounts in the sales, purchase and nominal ledgers.(b)Quite apart from that, Mr. Balch had the only credit card on the company's bank account and was registered with the bank for online banking in respect of the Company's account. This enabled him to know the exact state of the Company's account at any time and to make money transfers from the account, a facility of which to my knowledge he availed himself. This was all in accordance with the overall agreement as to how the Company was run, which was that the management of the business was to be a matter for him, for which he received a remuneration of £45,000 a year plus expenses.(c)The cheque book was kept at the office. The mandate was ‘either to sign’ and it was therefore in Mr. Balch's de facto control. This again was in accordance with the agreement as to how the business was to be run, as he would need it to make payments on the Company's behalf.(d)I did not work at the office at all. I did not have a desk there. I called in from time to time to see how things were progressing, and I also had access to the bank account via online banking so I could see the bank position at any time. I did not have access to the accounts software. I have a copy of it now because I retained a ‘back up’ copy when the books and records were handed over to the Official Receiver but I did not have any such copy whilst the Company was in operation. Mr. Balch of course raised any matters of significance with me when I called in or by telephone at other times, and I received printed reports and management accounts from time to time, but I did not make entries in the accounts or have day to day familiarity with the detail of them”.

24 In para.7 of his witness statement, the Defendant sets out why Mr. Balch's statement to the Official Receiver's examiner that he was responsible for the payment of VAT and PAYE and for dealing with HM Revenue and Customs is incorrect. I need not go through the reasons that the Defendant gives for disputing Mr. Balch's statement. I am satisfied that the substance of the explanation the Defendant gives is correct. It is supported by the documents he produces. I see nothing in what the Deputy Official Receiver says at paras.8 to 14 of her second report dated 21st August 2007 that detracts from this. In fact, in the course of giving her evidence, the Deputy Official Receiver realistically accepted that she could not seriously challenge the matters set out in para.6, and to some extent para.7 of the Defendant's witness statement.

25 The Official Receiver could have obtained the observations of Mr. Balch to those matters. However, he chose not to do so. It is surprising that he did not. If his case was premised — as it clearly was initially — on the basis that the Defendant was responsible for running the financial side of Riva's business, he ought to have made some attempt to obtain written evidence from Mr. Balch on which Mr. Balch could be cross-examined. He might at the very least have made enquiries of Elaine Lovett, who worked with Mr. Balch, to obtain further information about the respective roles and responsibilities of the two directors. The court might then have had a clearer picture as to their respective roles and responsibilities. It is not clear why he felt unable or unwilling to take this course of action.

26 Mr. Balch asserts that he had no responsibility for dealing with the financial side of Riva. The Defendant says the precise opposite. Each director attributes the responsibility for dealing with the financial affairs of Riva to the other. Each says that the other was responsible for paying the VAT and PAYE. Each thought that the other was doing so. Neither thought that the payments were not being made.

27 Where the respective positions maintained by the directors are so diametrically opposed, I consider what appears to be the Official Receiver's complete acceptance of the veracity of the information given to him by Mr. Balch — without conducting any or any proper enquires into the information given by Mr Balch — to be entirely inappropriate. I cannot see any reason why the Official Receiver should have accepted the explanation give to him by Mr. Balch in preference to that proffered by the Defendant. He ought to have made further enquiries about whether he could

accept what was being said by Mr. Balch before he decided to bring this claim.

28 I am unable to accept the assertion of the Official Receiver — if that still remains his position — that the main control of the financial affairs of Riva was in the hands of the Defendant. I consider that it was principally in the hands of Mr. Balch. It is clear to me that Mr. Balch has sought to underplay his role in his explanation to the Official Receiver about the manner in which the financial affairs of Riva were conducted. There is no dispute that Mr. Balch was in day to day charge of Riva and that the Defendant had little involvement in its day to day running.

29 Mr. Balch received remuneration for the services he provided to Riva, though there is a dispute as to how much he received. He says he received £40,000; the Defendant says that Mr. Balch received £45,000. At any rate, Mr Balch received remuneration for the services he provided to Riva — and given Riva's precarious financial position throughout its existence — substantial remuneration at that! The Defendant did not. Mr. Balch was the point of contact with HM Customs &Excise and also with the Inland Revenue for the purpose of the CIS tax scheme. The Defendant had little contact with them. Mr. Balch described himself as the managing director in correspondence and communication with H.M. Customs &Excise. That was because he was the managing director. I reject any suggestion that the Defendant — and not Mr. Balch — was primarily or principally responsible for the financial affairs of Riva.

30 It is clear that the Official Receiver now accepts that the position about who was running Riva may not be as clear-cut as he thought. On the first day of the trial last week, he sought my permission to amend the charges against the Defendant from alleging that the Defendant ‘caused’ Riva to trade to the detriment of the Crown and Curstons to alleging that the Defendant had ‘caused or allowed’ Riva to trade in that manner. He probably did not need to, having regard to the observations of His Honour Judge Roger Kay QC (sitting as a Deputy Judge of the High Court) in the Secretary of State v Kappler [2006] EWHC 3694 (Ch). However, he was right to do so, given the possibility that he might not be able to establish that the Defendant had actual knowledge of the matters alleged against him. The defence of the Defendant was, to a large extent, based on the fact that he was unaware of what was happening with regard to the withholding of repayments to the Crown and Curstons. I granted permission on the basis that the Defendant could not have been taken by surprise by the amendments. Despite reserving the Defendant's position in his written submissions, Mr. Whitaker realistically accepted that it was not appropriate for permission to be refused.

31 I am also unable to accept Mr. Balch's assertion that he resigned as a director of Riva on 5th July 2004. It is correct that in para.1 of a statement that he forwarded to the Official Receiver's office in August 2006, the Defendant mentioned that Mr. Balch had resigned in July 2004. I do not know why he said that. However, in the absence of evidence from Mr. Balch on the issue, I consider that the documents that the Defendant has produced in support of his assertion that Mr Balch had not resigned his directorship in July 2004 to be compelling. I am satisfied that Mr. Balch remained a director of Riva up until the date when it went into liquidation.

32 In addition, I am unable to accept Mr. Balch's version of the events that took place on 5th or 6th October. Although Mr. Capon on behalf of the Official Receiver attacked the assertion made by the Defendant that the Experian contract was completed by a company controlled by Mr. Balch, I see no reason, in the absence of any observations being obtained from Mr. Balch about the veracity of the information given by the Defendant, to doubt what the Defendant was saying. Indeed, there is no suggestion in the Official Receiver's second report that the information given is incorrect. I cannot see that whether Mr. Balch was sacked, as he alleges, or Riva simply ceased trading, as the Defendant alleges, has any bearing on the substance of the Official Receiver's claim. However, I consider that Mr. Balch's version of events as to what happened is less reliable than

the version put forward by the Defendant. Whether Mr. Balch was sacked, as he alleges, or the business was closed down, as the Defendant alleges, there is no issue that Riva had all but stopped trading at the time.

33 It is appropriate, before I deal with whether the charges are made out, I give a short summary of the legal position that applies in the present case. I have already referred to s.6 of the Company Directors Disqualification Act 1986 . In deciding, pursuant to s.6(1)(b) , whether a person's conduct as a director makes him unfit to be concerned in the management of a company, section 9 of the Act specifies by reference to schedule 1 those matters to which the court is required to have regard. However, it is clear that the provisions of s.9 in schedule 1 to the Act are not exhaustive and the court can consider any misconduct of the director in deciding whether he is unfit, see, for example, the observations of Neuberger J in Re Amaron Limited, Secretary of State for Trade &Industry v Lubrani (No. 2) [2001] 1 BCLC 562 at 568.

34 The approach that the court needs to take in determining whether unfitness has been established has been variously stated in different cases. One exposition of the test to be applied is to be found in Re Grayan Building Services Limited, Secretary of State for Trade &Industry v Gray [1995] 1 BCLC 276 . Hoffman LJ (as he then was) said (at p 284) that the function of the court was, as he put it, "to decide whether [the defendant's] conduct, viewed cumulatively, and taking into account any extenuating circumstances, has fallen below the standards of probity and competence appropriate for persons to be directors of companies."

35 The approach that the court needs to adopt in determining whether the requirements of s.6(1)(b) have been met were summarised by Blackburne J in Re Structural Concrete Limited Official Receiver v Barnes [2001] BCC 578 at 596. He mentioned that the decision involved a three stage process. First, do the matters relied upon amount to misconduct? Second, if they do, do they justify a finding of unfitness? And, third, if they do, what period of disqualification, being not less than two years, should result? I respectfully agree with, and gratefully, adopt that summary.

36 The burden of proving unfitness lies on the Official Receiver. Although the proceedings are civil, nevertheless the burden is, as Jonathan Parker J said in Re Barings plc (no 5), Secretary of State for Trade &Industry v Baker [1991] 1 BCLC 433 at 484, a "heavy one." The reason for that is the disqualification proceedings are serious in nature being, as is often said, of a penal or quasi penal nature.

37 Dillon LJ in Re Sevenoaks Stationers (Retail) Limited [1991] Ch 164 at 176 stated that the words "makes him unfit to be concerned in the management of a company" were "ordinary words of the English language … [that] should be simple to apply in most cases and that "it was important to hold to those words in each case." The Court of Appeal decision in Re Grayan makes it clear that a judge having to consider whether a defendant is unfit is deciding a question of mixed fact in law. What the court is required to do, in essence, is as Lewison J said in Secretary of State for Trade &Industry v Goldberg [2004] 1 BCLC 597 , to take a broad brush approach in making a value judgment about a defendant's fitness or otherwise to be a director by applying the facts of the case to the standard of conduct laid down by the court appropriate to be a person fit to be a director. As has been pointed out in *Mithani: Directors' Disqualification* at para. **II [344]** , the making of that value judgment requires little more than for a court to come to a common sense decision about whether the facts of the case when applied to the standard of conduct laid down by the court should result in a finding of unfitness being made against a defendant.

38 In determining unfitness, the court can only look at the specific allegations that have been made by the claimant — in this case the Of-

ficial Receiver — in his evidence in support of the application for the disqualification order against the Defendant, though the allegations themselves need not be framed with the precision of criminal charges. It is not appropriate for the claimant to rely on conduct, or allegations not made in that evidence, see for example, Re Grayan Building Services Limited, Secretary of State for Trade &Industry v Gray [1995] 1 BCLC 276 at 284.

39 The principal allegation of misconduct which it is asserted establishes unfitness in this case is that the Defendant caused or allowed Riva to trade to the detriment of the Crown. It has long been established that non-payment of Crown debts is no more serious than a failure to pay other creditors. The principle was firmly established in Sevenoaks . In that case Dillon LJ, having confirmed that non payment of Crown debts could not be treated as automatic grounds for disqualification then went on to say ([1991] BCLC 325 at 337):

"… what is relevant in the Crown's position is not that the debt is a debt which arose from a compulsory detachment from employees' wages, or a compulsory payment of VAT, but that the Crown was not pressing for payment and the director was taking unfair advantage of that forbearance on the part of the Crown, and, instead of providing adequate working capital was trading at the Crown's expense while the companies were in jeopardy. It would be equally unfair to trade in that way and in such circumstances at the expense of creditors other than the Crown".

40 The allegations of misconduct in the present case are primarily based upon unfair discrimination. In essence, the first charge is that the Defendant unfairly discriminated against one creditor, the Inland Revenue, a Crown creditor, in favour of other — or another class of — creditors, namely certain trade creditors, and in particular Art Stone, a company owned or controlled by the Defendant. The essence of the second charge is also the same. The Defendant is alleged to have caused Riva to trade to the detriment of Curstons, in that despite Riva being indebted to Curstons in the sum of £20,960 by September 2004, no attempt was made to make any payment of this sum, and monies received by Riva in August and September 2004 were paid out to other creditors, including Art Stone.

41 As I have said, the basis of the allegation is that Riva has deliberately chosen to withhold payment to a creditor, whether for commercial or other reasons, which it does not regard as pressing or essential in allowing it to continue trading. The decision to withhold payment might be, and often is, down to the fact that the creditor has not chased for the payment, or that the procedures for collection of the amount due to him are inadequate or insufficient. However, I agree with Mr. Capon, that it may also be due to other reasons, for example, the company does not regard the payment of the debt to be of any significant importance to it; or it wishes to pay a director or persons connected with a director; or to make payment to reduce the liability or prospective liability of the director to the company's bank under a guarantee given by the director to the bank. Indeed, the period during which payments are alleged by the Official Receiver in the second charge to have been withheld from Customs was at a time when Curstons were pressing for payment. That makes them pressing, in the sense that they were pressing for payment, but not pressing in the sense that Riva regarded payment to them as being pressing or essential.

42 It is a necessary ingredient of the charge of causing the company to trade to the detriment of a creditor that the company should have pursued a deliberate policy of payment that has discriminated against such a creditor. In the words Neuberger J in Re Verby Print for Advertising Limited [1998] BCLC 23 at 29:

"[Counsel for the defendant] contended that before unfair discrimination against a creditor can justify a finding of unfitness under the 1986 Act there must be an actual policy of discrimination … It is accepted on behalf of the Secretary of State that a policy for unfair discrimination between creditors must be established before a

finding of unfitness can be justified in a case such as this. I consider that concession is right if the word ‘policy’ is given its normal meaning. That is because the concept of a policy or some sort of decision; the decision may be conscious or sub conscious, and the reasons for it may be conscious or unconscious. Without there having been a policy of discrimination, it is difficult to see how the discrimination could be unfair and it necessary for the discrimination to be unfair, as I read from the judgment of Dillon LJ, before it can give rise to a finding of unfitness.”

43 Whether the Official Receiver's claim against the Defendant succeeds must, to a large extent, depend upon whether a proper inference can be drawn — from the accounting and other records of Riva, the pattern of payment made by Riva to its creditors, and from the explanation that the Defendant provided — that Riva operated a policy of discrimination. No part of the Official Receiver's case is based upon any information given to him by Mr. Balch that such a policy existed. Indeed, if such was the case, it is likely that Mr. Balch would also be responsible for causing the policy to be operated — or at least allowing it to be operated — and would have been subject to these proceedings in the same way as the Defendant.

44 It is clear from Riva's books and records that a substantial amount of PAYE and NIC was deducted from its employees. Riva should have accounted for the deductions it made to the Inland Revenue subject, of course, to any adjustments that it was able to make on account of any credit to which it was entitled in respect of CIS payments deducted by the main employer. The amount that it should have paid over to the Inland Revenue was some £28,000 to take into account CIS credits, including the credit for the sum of £5,000, to which I have already referred. The only payments, however, that Riva made to the Inland Revenue in respect of that liability were £307.91 on 18th December 2003, and £1,076.22 paid on 10th February 2004.

45 Riva fell into arrears during its first eight months of trading in the 2003 to 2004 tax year. Riva failed to make any payment to the Inland Revenue from 10th February 2004 until it ceased trading in September 2004. However, it made payments to other creditors, including Art Stone. The Official Receiver contends that the clear inference from this must be that a decision was — or decisions were made — not to make further payment to the Inland Revenue.

46 The Defendant accepts that he knew in July 2004 that Riva was struggling, which meant that Riva would probably also have been struggling to account for PAYE and NIC. The Official Receiver asserts that his failure to do so, while making payments to other creditors, including his own company, demonstrates, that he adopted a policy of discrimination against the Inland Revenue in favour of other creditors.

47 The Defendant maintains that he had little involvement in the financial side of the business and was not involved in any decision about who should get paid and who should not, at any rate until July 2004, when he came to find out Riva's precarious position. At para.25 of his witness statement he says this:

“However, I would emphasise that: (a) I was not directly responsible and believed everything was operating normally until June/July 2004; (b) I accept that after that date I knew the company was struggling because of adverse conditions on the Experian contract. If asked, I would certainly have thought that I presumed that this included struggling to account for PAYE and NI, although I would also have said that CIS could take care of the greater part of that”.

48 The Defendant went further in the course of giving his evidence. He said that up until July he had been assured by Mr. Balch that Riva was paying the Inland Revenue. He said that he had no reason to believe that what he was being told by Mr. Balch was untrue. Mr. Whitaker contends that if I accept what the Defendant says then it is not possible for me to find that the Defendant caused or allowed Riva to operate a policy of discrimination, at any rate before July 2004. He contends if there was a policy of discrimination it was not the Defendant's policy of discrimination;

it was Mr. Balch's policy and the Defendant was wholly unaware of it.

49 The Official Receiver, on the other hand, contends that even if the Defendant says he did not know that the Inland Revenue was not being paid, he ought to have known that it was not. He had the means to find out, and cannot rely on his failure to discharge his duty to monitor and supervise the financial affairs of Riva as an excuse to escape a finding of unfitness in such circumstances.

50 Mr. Capon relies on a number of well-authorities in this area: Re Barings plc [1999] 1 BCLC 433 , Re Park House Properties Limited [1997] 2 BCLC 530 , Re Burnham Marketing Limited [1993] BCC 518 at 526 to 528, and Secretary of State for Trade &Industry v Thornbury [2008] 1 BCLC 139 . I agree with Mr. Capon. The Defendant is unable to rely upon his apparent lack of knowledge of the financial affairs of Riva as an excuse to escape a finding of unfitness. Accordingly, he cannot escape a finding of unfitness on the basis that he was unaware of what was going on. He ought to have known what was going on.

51 In any event, I do not accept what the Defendant says. I am unable to accept that up until July 2004, the Defendant had been assured by Mr. Balch that Riva was paying the Inland Revenue and that had no reason, therefore, to think that payments were being withheld from them. He made no mention of this in his witness statement. There would have been no reason at all for Mr. Balch to lie to him. It is also surprising that he does not appear to have taken this up with Mr. Balch when he found out that Mr. Balch had allegedly lied to him. I am in no doubt that it would have been obvious to the Defendant that the Inland Revenue was not being paid. The Defendant was seeking to do in the course of giving his evidence what Mr. Balch had sought to do when providing information about the affairs of Riva to the Official Receiver's examiner. He was seeking to shift the blame for the mismanagement of the financial affairs entirely on to Mr. Balch.

52 However, the question for determination by me is whether the charge is made out. It is correct that PAYE and NIC deductions were not being handed over to the Inland Revenue. However, it is also correct that Riva was not making payment to a number of its other creditors. Mr. Capon says that the failure by Riva to make payment to other creditors should not by itself preclude a finding of a policy of discrimination from being made. I agree with that proposition. However, in the present case, Riva was treating a great number of its creditors in the same disdainful and dismissive manner as it was treating the Inland Revenue.

53 In para.27 of the Defendant's witness statement, he sets out details of a number of other creditors who were treated in a manner similar to the Inland Revenue. They included the following:

- (a) The petitioning creditor, CCF Limited, to whom nothing was paid. They were owed £5,400 odd. Their debt dated back to June/July 2004.
- (b) Guardian Glazing Films Limited to whom nothing was paid. They were owed £8,629.27 for goods supplied to the Experian job in August and September 2004.
- (c) Lee Glass to whom only some £1,500 was paid out of a total value of goods supplied to the Experian job of some £28,000. Lee Glass were the largest trade creditors of Riva. The Defendant observes that the assertion that Curstons were being ignored must at the very least — when compared to the manner in which Lee Glass were treated — demonstrate that that the OR's assertion cannot be correct.

54 The Official Receiver's response to that is twofold. First, to summarise, the manner in which the changes in the amounts due and owing to trade creditors on the one hand and the Revenue on the other hand took place over the period from August 2004 to December 2004. That summary is contained at p.218 of the bundle. I find little there to assist me. All the summary shows is that trade creditors on the whole fared better than the Revenue. However, that is not the charge that the Defendant has to answer.

55 The other is to invite me to ignore, for the pur-

pose of considering whether there was a policy of discrimination, any failure to pay creditors whose debts had not become due. I am unable to accept that. In the first place, there is no evidence as to what Riva's terms of credit were with some of these creditors. However, it seems to me to be artificial simply to say that in deciding whether there was a policy of discrimination, once simply ignores recent creditors or creditors who are not paid because their debts may not have been due for payment. That supposes that those creditors would be paid if their debts had become payable in preference to the debts of those, such as the Crown, against whom there is alleged to have existed a policy of discrimination.

56 It is clear to me that Riva would not have paid those creditors even if their debts had become payable. By about September 2004, all Riva appeared to be concerned about was paying what was absolutely necessary in order to enable it to receive payments on its outstanding contracts. This is borne out by the dismissive manner in which the Defendant dealt with Curstons, even though at the time Curstons were pressurising Riva to pay their account. It left a number of creditors — in addition to the Inland Revenue — unpaid in order to further that objective.

57 When the accounting and other records of Riva are properly analysed, the pattern of payments made by Riva to its creditors properly considered, and the explanation provided by the Defendant properly evaluated, there is no evidence of any policy of discrimination. Riva treated a number of its major or significant suppliers in the same unconcerned, uncaring and dismissive manner as it treated the Crown. I cannot see any policy of discrimination established on the facts. Indeed, the Deputy Official Receiver herself said when giving evidence that the reason that the Defendant was singled out for treatment by the Official Receiver was that he had, to use her word, ‘preferred’ Art Stone. I agree with her. That is the real nature of the charge against the Defendant.

58 Mr. Capon was quick to point out that the fact that a creditor might be preferred should not preclude a finding of a policy of discrimination being made. I agree with him. Indeed, Verby is clearly authority for that proposition, and also for the proposition that such payments may need to be taken into account in deciding whether a policy of discrimination was in existence. However, the Official Receiver's real complaint about the withholding of payments to the Crown is less to do with any policy of discrimination and more to do with the making of payments to Art Stone liable to be set aside as preferences under s.239 of the Insolvency Act 1986 .

59 Mr. Capon, quite properly, steered away from any questioning or cross-examination on that subject — no doubt because it forms no part of the Official Receiver's claim against the Defendant. However, I cannot help feeling that had the Official Receiver included a charge based on preference, or some other similar type of misconduct, and concentrated his enquiries on those areas of conduct of the Defendant, there would have been a more compelling case for the Defendant to answer.

60 I can deal briefly with the allegation that concerns trading to the detriment of Customs. During June, July and August 2004 Riva was invoiced for good supply to it by Customs. By 31st July 2004, Riva owed Customs some £20,000 of which £16,000 was due for payment. By 31st August 2004, Riva had been invoiced a further £785.51 for goods, and some £20,000 was due for payment. Despite the invoices from Curstons going back to 10th June, Riva made no payments to Curstons in respect of these goods. Promises of payment were made to Curstons by Riva on 5th, 11th, 17th and 19th August 2004. On 19th August, the Defendant assured Curstons that payment would be made by 27th August 2004. On 1st September, the Defendant made a further promise of payment by 10th September 2004 but no payment was made.

61 During August 2004, Riva received a number of payments into its bank account. They totalled a sum in excess of £72,000. During September 2004, Riva received a further £71,000 into its bank account. The receipt of funds by Riva on

27th August and 10th September matched promises of payment made by the Defendant to Curstons. Notwithstanding these promises, and the receipt of funds by Riva, no payments were made to Curstons. Instead, payments were made to other creditors and to Art Stone. These payments are set out at paras.53 to 59 of the Deputy Official Receiver's first report.

62 Various issues arise between the Official Receiver and the Defendant about the relationship of the two companies. They include issues about the manner in which the advances were made, their purpose, whether they were made directly to employees or made to Riva for the purpose of paying wages, how they were repaid, whether there was any overpayment, whether Riva is a creditor or debtor of Art Stone, the nature of Art Stone's claim in the liquidation, and, if it is found to be a creditor of Riva, whether it might have a preferential claim on the basis of having paid wages and therefore subrogated to the claims of some of the employees.

63 The Official Receiver alleges that the Defendant was directly involved in the discussions with Curstons and made specific promises of payment to them, which Curstons relied upon in deferring legal proceedings against Riva. In the circumstances, it is asserted that an inference should be drawn that a decision was taken not to pay Curstons and the failure to make any payment to Curstons was unfairly prejudicial to them. I agree with the Official Receiver that the manner in which the Defendant behaved towards Curstons was appalling. However, I cannot see anything from the evidence of the Official Receiver that suggests that Riva discriminated against Curstons. As I said earlier, it treated them in the same disdainful manner as it treated a number of its other creditors. The allegation amounts to no more than an assertion that the Defendant made promises to pay Riva's indebtedness to Curstons but did not keep those promises. When one adds to that the threat of legal proceedings that were made by Curstons and simply ignored by Riva, it is difficult to see how Riva could be said to have discriminated against Curstons, or to have acted in a manner specifically prejudicial to the Defendant as against any of its other creditors.

64 It is significant that the charge only relates to the period between August and September 2004. Of course, I accept that this by itself does not preclude a finding of a policy of discrimination or prejudice against a specific creditor. However, it is also right to point out that in Verby, at [1998] 2 BCLC 23 at 39 Neuberger J observed:

“Clearly, the shorter the period during which the policy exists, the less grave a view the court may take of the policy, all other things being equal.”

65 In addition, *Mithani: Directors' Disqualification* contains the following passage at **II [697E]** :

“Even though there is no minimum period during which the failure to make payment of non-pressing debts is required to subsist, where the amount outstanding to him is small, or a tiny fraction of the company's deficiency, the failure to pay him will probably not be regarded as amounting to a policy of discrimination. Similarly, where the non-pressing debts have accrued over a short period of time or are recent or do not form a substantial proportion of the company's total deficiency, the court may be reluctant to conclude that the directors deliberately delayed their payment and used them as working capital. It will be otherwise where the debts are large and have been allowed by the directors to accumulate at a time when the company is getting into greater financial difficulties or is insolvent.

Where the amounts to the non-pressing creditors have remained constant over the company's period of trading, it is unlikely that a policy of discrimination will be found to have existed.

Various authorities are given in the footnotes to this passage in support of these propositions. It is not necessary for me to go through them.

66 I do not find the second charge made out either.

67 However, even if I were incorrect in my as-

sessment of the evidence and had found that misconduct in the form of the existence of a policy of discrimination had been established, I would have had not hesitation in finding that the conduct of the Defendant was not unfit. In the context of the charges brought against — and it can only be in that context and not in any wider context — I cannot see how the Defendant could be said to be unfit even if he had been found to be guilty of the allegations made against him.

68 In the first place, although Mr. Balch was — as I have found — the managing director of Riva and primarily responsible for managing its financial affairs, including dealing with the Inland Revenue, the Official Receiver chose not to bring any proceedings against him. Whether he was right not to do so is not for me to say. The Official Receiver's decision appears to have been influenced by the various — what the Deputy Official Receiver described as — 'preference payments' made to Art Stone in which she correctly indicated Mr. Balch had no interest. If that was the only reason — and it appears to have been the only reason from the evidence the Deputy Official Receiver gave — the decision not to include Mr Balch in these proceedings seems to me, to say the least, strange. I do not see why a distinction between them should have been made in the context of these charges on that basis alone.

69 Mr. Balch was the Managing Director of the Riva and obtained what in the context of the financial position of Riva was a substantial salary. It seems to me — and I can only express a provisional view because, quite rightly, there was no detailed questioning on the point — that Riva had always been insolvent. The salary that he received, together with his expenses, were paid to him almost up to the date that Riva ceased trading. The Defendant on the other hand received no reward for the limited services he provided to Riva. In addition, Mr. Balch took over the benefit of the last stages of the Experian contract with the possibility that he received some benefit from it.

70 In Re Dawson Print Group Limited [1987] BCLC 601 at 604, Hoffman J considered, in the context of an application made to disqualify a director under the discretionary power to disqualify contained in the previous legislation on the subject, s.300 of the Companies Act 1985 , that, to use his words:

"The Official Receiver tries to deal with each case on its merits. Nevertheless, looking at it from the point of view of the director on the receiving end of such application, I think that justice requires that he should have some grounds for feeling that he has not simply been picked on."

71 Of course, the provisions of s.6 are vastly different from those of s.300 . For a start, under s 6 , there is a duty to disqualify a defendant if his conduct is found to be unfit. The court does not have discretion. Under s 300 , the court had a discretion to disqualify and it could always refuse to exercise its discretion where the circumstances justified its taking that course of action.

72 It follows, therefore, that ordinarily, the decision to leave out from proceedings a director whose conduct is at least as culpable as one against whom proceedings are taken will be of little consequence to the value judgment that the court needs to make about the fitness or otherwise of the director against whom proceedings have been taken. However, I see no reason why in an appropriate case — and this is such a case — the court should not take into account the deliberate exclusion from proceedings of a director against whom there is at least an equally compelling case in coming to its value judgment about the Defendant's fitness to be involved in the management of company. In the present case, the Official Receiver has chosen to bring proceedings against one director only in circumstances where: (a) there was clear evidence available to him that the conduct of the other director was at least as — if not more — blameworthy; (b) the evidence against the Defendant was based almost entirely on information provided to the Official Receiver by the other director, which the Official Receiver accepted at face value and took few steps to in-

vestigate independently; and (c) the basis upon which the Official Receiver sought to apportion the responsibility between the two directors in the allegations made by him were misconceived. I consider that, in such circumstances, the court should be careful before concluding that the director against whom proceedings have been taken was unfit. If the possibility of the conduct of the other director being unfit never entered into the claimant's mind or if having considered it, he nevertheless thought that there was no evidence to justify a finding of unfitness against them, the court should carefully consider whether the claimant could properly have taken the view that the conduct of the director against whom proceedings were taken was unfit. In the present case, the basis upon and the circumstances in which the Official Receiver decided to proceed against the Defendant would leave the Defendant legitimately aggrieved that he was being unfairly singled out for action by the Official Receiver. He is entitled to invite the court, in the circumstances, to consider whether the Official Receiver could properly have formed the view that he was unfit when he had formed the opposite view with regard to the other director. In the present case, it is difficult to see how he could have formed that view.

73 However, that is not all. It is correct that Riva is alleged to have made inappropriate payments to Art Stone. However, that is not the charge that the Defendant has to face. In the limited context of the actual charges made against the Defendant — that of operating a policy of discrimination — he cannot be said to have received any, or any substantial reward for the investment he made in Riva. He cannot be said in, the present case, to have lined his own pockets. He may have attempted to obtain some personal benefit by paying himself £10,000 when he realised that Riva was in serious financial difficulty. He said that he paid himself that amount to reimburse himself for the goods that he had purchased on behalf of Riva which had not been recorded in the accounting records of Riva. Although I do not accept what he says, he had the foresight to repay it back immediately knowing that whatever the purpose of the payment, it was wholly inappropriate and almost certainly likely to be challenged by a liquidator

74 It follows, therefore, that even if I had come to the conclusion — which of course I have not — that misconduct on the part of the Defendant had been established, I cannot see how that misconduct would in the present circumstances have amounted to unfitness.

75 The application is therefore dismissed.

76 It is right, however, that I make one final observation. I find it, to say the least, surprising that the Official Receiver did not think it appropriate to bring other charges against the Defendant arising out of the collapse of Riva. There would have been a compelling case for the Defendant to answer if the Official Receiver had decided to include in his claim a charge based on preference, or some other similar type of misconduct, or trading at the risk or to the detriment of creditors generally, or failing to supervise or control the proper running of Riva. Indeed, on 18th October 2004, being the date when the winding up petition against Riva was presented, Riva paid a sum of £5,000 to K.T. Joinery. The payment went through Riva's bank account on 5th November 2004. That payment might itself have been included in the claim as a separate charge — as being a transaction liable to be set aside under s.127 of the Insolvency Act 1986 — and therefore requiring specifically to be considered by the court under para.8(a) Part 2 of Schedule 1 to the 1986 Act. In addition, Mr Capon drew my attention to various other companies in which the Defendant had directorships which had gone into an insolvent process or had ceased trading. The Official Receiver might also have thought it appropriate to include those companies in these proceedings as ‘collateral companies’. However, he chose not to do so.

77 It is necessary for the Claimant — whether it be the Secretary of State or the Official Receiver — to be particularly vigilant in the way in which he casts his charges against a defendant. The Claimant has to be careful in ensuring that the evidence upon which he relies properly supports the charge that his making against a defendant.

Where the evidence might support a number of charges he ought to make sure, consistently with his duty to act fairly, that all the charges it supports are included in the claim that he makes against a defendant where appropriate, in the alternative. His failure to do so might result in the dismissal of the claim when, as appears to be position in this case, there might be a compelling case for the defendant to answer had other charges been brought against him.

78 There is no reason why the charges I have mentioned, and other appropriate charges, could not have been included in the claim. The Official Receiver might have been justified initially in proceeding on the present charges only. However, it is necessary for him, or the Secretary of State, to keep under constant review the basis of the allegations that are made against a director.

79 Where in the course of the evidence disclosed by a defendant it becomes apparent that the charges the claimant has brought against a defendant ought to be supplemented or modified, he should seek permission to do so consistently, of course, with his duty to act fairly. This is not necessary just because it is essential for the evidence relied upon by the claimant to support the charges that the claimant can properly make up, but also because the public is entitled to expect that the claimant will ordinarily include in the claim all the charges that he has a reasonably prospect of establishing against a defendant in order that any disqualification period imposed upon a defendant is commensurate with the conduct alleged against him.

80 It does seem to me, in the circumstances of the present case, that the public is legitimately entitled to feel that it has been let down by the manner in which the Official Receiver has sought to formulate the charges against the Defendant. A disqualification order for a lengthy period might have been imposed against the Defendant if the charges against him had been properly formulated.
END OF DOCUMENT